

Columbia Law School

Scholarship Archive

Faculty Scholarship

Faculty Publications

2017

Class Actions in the Era of Trump: Trends and Developments in Class Certification and Related Issues

John C. Coffee Jr.

Columbia Law School, jcoffee@law.columbia.edu

Alexandra D. Lahav

alahav@law.uconn.edu

Follow this and additional works at: https://scholarship.law.columbia.edu/faculty_scholarship



Part of the [Securities Law Commons](#), and the [Torts Commons](#)

Recommended Citation

John C. Coffee Jr. & Alexandra D. Lahav, *Class Actions in the Era of Trump: Trends and Developments in Class Certification and Related Issues*, (2017).

Available at: https://scholarship.law.columbia.edu/faculty_scholarship/2055

This Working Paper is brought to you for free and open access by the Faculty Publications at Scholarship Archive. It has been accepted for inclusion in Faculty Scholarship by an authorized administrator of Scholarship Archive. For more information, please contact cls2184@columbia.edu.

**Class Actions in the Era of Trump:
Trends and Developments in Class Certification and Related Issues**

John C. Coffee, Jr. and Alexandra D. Lahav

September 15, 2017

This Memorandum has been prepared for the Annual American Bar Association National Institute on Class Actions, to be held this year in Washington, D.C. on October 26-27, 2017.

CLASS ACTIONS IN THE ERA OF TRUMP

Trends and Developments in Class Certification and Related Topics



By John C. Coffee, Jr. and



Alexandra D. Lahav

September 1, 2017

Professor John C. Coffee, Jr. is the Adolf A. Berle Professor of Law at Columbia University Law School. Professor Alexandra D. Lahav is the Ellen Ash Peters Professor of Law at the University of Connecticut. Professors Coffee and Lahav retain the copyright to this article.

<u>A.</u>	<u>SECURITIES LITIGATION</u>	<u>4</u>
A.	OVERVIEW	4
B.	STATUTES OF REPOSE	5
C.	STATUTE OF LIMITATIONS FOR SEC DISGORGEMENT	8
D.	SLUSA AND FEDERAL SECURITIES CLASS ACTIONS IN STATE COURT	8
E.	WHEN ARE OMISSIONS OF INFORMATION ACTIONABLE UNDER RULE 10B-5	10
F.	PREDOMINANCE	11
G.	RELIANCE AND THE “FRAUD-ON-THE-MARKET” DOCTRINE	12
H.	CONFIDENTIAL WITNESSES IN SECURITIES LITIGATION	15
<u>II.</u>	<u>ASCERTAINABILITY</u>	<u>20</u>
<u>III.</u>	<u>JUSTICIABILITY</u>	<u>26</u>
A.	STANDING	26
B.	MOOTNESS	31
<u>IV.</u>	<u>CHANGES TO RULE 23</u>	<u>33</u>
<u>V.</u>	<u>APPEALS OF CLASS CERTIFICATION ORDERS</u>	<u>35</u>
<u>VI.</u>	<u>INJUNCTIVE CLASS ACTIONS</u>	<u>36</u>
<u>VII.</u>	<u>AFTER THE SETTLEMENT: FEES AND THE DISTRIBUTION PROCESS</u>	<u>38</u>
A.	ATTORNEY’S FEE AWARDS.	38
B.	HOLDBACKS AND PROPOSED RULE 23(E)(2)	40
C.	SMALLER CLAIMANTS AND EQUITABLE DISTRIBUTION	41
D.	CY PRES RECOVERIES	44
E.	INJUNCTIVE RELIEF IN CONSUMER CLASS ACTIONS	45

Introduction

2017 is the first year of the Trump Administration, and it was reasonable to expect major changes in (or at least attacks on) the contemporary law on class actions. But, so far, these attacks have fizzled. To be sure, the House of Representatives did pass the “Fairness in Class Action Litigation Act of 2017” (H.R. 985) by a close, party-line vote, and it would have significantly cut back on class actions (including by restricting the ability of a plaintiff’s attorney to represent the same client in a class action more than once).¹ That legislation has gone nowhere in the Senate, and because it seems unlikely to pass, we will not analyze it in this memorandum.

Similarly, the Supreme Court has not granted certiorari in any major class action case, but it has granted cert in related cases. Three consolidated cases involving the relationship between the Federal Arbitration Act and the National Labor Relations Act will likely decide whether employees will be able to proceed collectively against employers or be required to arbitrate their claims individually; these cases will be heard at the Court’s first session in October this term.² Overall, decisions at the Circuit Court level have been mixed, but no issue has yet surfaced that would materially change the class action status quo. The effect of recent decisions involving standing and mootness on class action practice have been minimal so far. A possible exception to this generalization involves the issue of “ascertainability,” an implied requirement for class certification, where the Circuits are sharply divided. As of this writing, a petition for certiorari raising this issue is pending before the Court.

¹ For a brief review of these provisions, see John C. Coffee, Jr. “How Not to Write a Class Action Reform Bill,” New York Law Journal, February 17, 2017.

² These cases are: Ernst & Young LLP v. Morris, Epic Systems Corp. v. Lewis, and National Labor Relations Board v. Murphy Oil USA, Inc. The Court has also granted certiorari on the question of the limits of state court jurisdiction over securities claims under the ‘33 Act. Cyan v. Beaver County Employees Retirement Fund, No. 15-1439, which is later discussed.

The Federal Rules Committee has approved a modest reformation of Fed. R. Civ. P. 23, but its changes, while important to practitioners, are characteristically marginal in their likely impact.

Of course, this period could be the “calm before the storm,” but we see little evidence of any sweeping changes. Indeed, in some areas (such as securities litigation) the rate of class action filings has recently soared. But the reasons for this surge are complicated. We give special attention in this memorandum to the context of securities litigation because it has seen a higher level of activity in overall filings, cases before the Supreme Court, and Circuit Court decisions.

A. SECURITIES LITIGATION

A. Overview

During the first half of 2017, securities class action filings soared to 246 cases (well above the average rate of 235 cases filed annually over the past five years). As many as 500 filings could occur this year if this trend persists (only the 508 cases filed in 2001 exceeds this level).

What is driving this growth? Although multiple explanations are possible, the clearest catalyst is the tendency of “merger objection” cases to migrate from state court to federal court (where they often seek federal jurisdiction based on alleged violations of the federal proxy rules). This may be a response to Delaware’s encouragement of “forum selection” clauses (which the Delaware Corporations Code now expressly authorizes). These clauses require any suit alleging a breach of a fiduciary duty in the case of a Delaware corporation to be filed in Delaware. Because the Delaware case law is extremely critical of “disclosure only” settlements (in which, by definition, there is no cash payment, except to the plaintiff’s attorneys) and will generally not permit fee awards in such cases,³ plaintiff’s counsel is motivated to avoid Delaware and sue in federal court (where the forum selection clause cannot apply). NERA Consulting estimates that one in five securities class actions filed in 2016 were “merger objection” cases,

³ See *In re Trulia, Inc. Shareholder Litigation*, 129 A. 3d 884 (Del Ch. 2016). Chancellor Bouchard did except cases in which the supplemental disclosures required by the settlement were “plainly material.” These, however, are rarer than unicorns.

and that this percentage will be substantially higher in 2017.⁴ Seemingly, the desire to avoid Delaware is flooding the federal courts with securities cases.

Nonetheless, Delaware's strategy may be working, as in 2016 of all public mergers valued at over \$100 million, only 73 percent of these deals attracted litigation—the lowest rate since at least 2009.⁵

The median settlement in the first half of 2017 was \$5.5 million, well below the median settlement for the last dozen years. This may again reflect the prevalence of “merger objection” cases, which typically settle on a “disclosure only” basis.

B. Statutes of Repose

In CalPERS v. ANZ Securities, Inc.,⁶ the Supreme Court resolved a Circuit split and curtailed its prior ruling in American Pipe & Construction Co. v. Utah,⁷ to hold that the filing of a class action does not toll the 3-year statute of repose in Section 13 of the Securities Act of 1933. Section 13 establishes a one and three year statute of limitation for alleged violations of Section 11 of the 1933 Act: one year after discovery of the untrue statement, or “after such discovery should have been made by the exercise of reasonable diligence,” but in no event more than three years after the sale of the security. In American Pipe, the Court had permitted the filing of the class action to toll the one year period, but in CalPERS, it has found that there can be no equitable tolling of the three year period. While American Pipe still applies to the one year period, the three year period is now an absolute bar. This means that if a class action settles after year three, no class member may at that point opt out and file an individual action (which is what plaintiff CalPERS had attempted to do in this case growing out of the Lehman Brothers bankruptcy).

⁴ See Stefan Boetttrich and Svetlana Starykh, Mid-2017 Flash Update (finding that “merger objection” cases brought in federal court rose from 30 in the first half of 2016 to 58 in the second half and then to 104 in the first half of 2017) (NERA Consulting).

⁵ See Matthew D. Cain, et al., The Shifting Tides of Merger Litigation, (available at: https://papers.ssrn.com/abstract_id=2922121) at 5-6.

⁶ 137 S. Ct. 2042 (2017)

⁷ 414 U.S. 538 (1974)

Almost certainly, this rule will similarly apply to the statute of limitations for Rule 10b-5 litigation (where the statute of limitation is two and five years).⁸ Also, it is likely to apply outside the federal securities context to other statutes having a statute of repose provision (or arguably having one). Thus, how does one determine if a limitations period in a statute represents a statute of limitations (and thus is subject to equitable tolling) or a statute of repose (and thus is not)? Writing for the 5-4 majority, Justice Kennedy found that statutes of limitations generally run from “‘when the cause of action accrues’—that is, ‘when the plaintiff can file suit and obtain relief.’”⁹ In contrast, statutes of repose “begin to run on ‘the date of the last culpable act of omission of the defendant’”¹⁰—such as the sale of the security. This distinction is likely to be litigated in future cases that provide only a single period of limitation.

The practical consequence of CalPERS is that many institutional investors will want to file a parallel individual action (which will likely be consolidated with the class action) before the three or five year statute of repose period runs out. It is likely that both sides will agree to let this suit lie dormant (both to economize on legal costs and because defendants would rarely want an individual suit to come to trial before the class action was resolved, as it could arguably give rise to offensive collateral estoppel).

A more troubling question involves how class counsel should respond to the approach of the three or five year statute of repose period. Often, the class action will not have been resolved by this period. In her dissent, Justice Ginsberg noted:

“As the repose period nears expiration, it should be incumbent on class counsel, guided by district courts, to notify class members about the consequences of failing to file a timely protective claim.”¹¹

⁸ See 28 U.S.C. §1658(b). Indeed, the Third Circuit has just so held, finding that CalPERS implies that the repose period (5 years) under the Exchange Act also cannot be equitably tolled. See North Sound Capital LLC v. Merck & Co., 2017 WL 327886 at *1 (3d Cir. August 2, 2017).

⁹ 137 S. Ct. at 2049.

¹⁰ *Id.*

¹¹ 137 S. Ct. 2042 at 2058.

This will be costly, but her comment suggests that district courts could require it. Notice of any proposed settlement will probably also have to indicate whether opting out is still feasible (in terms of whether an individual action can be filed).

As Justice Ginsberg further noted, one impact of CalPERS may be to slow down the settlement process, as defendants may prefer to settle only after the statute of repose has expired (in order to limit opt outs to those who had earlier filed an individual action). This is debatable. Others believe that most institutional investors are sophisticated and will file a parallel action as a matter of course (in which case delay would achieve little for defendants). But this remains to be seen, as smaller institutions may not want to incur the costs of filing an individual action, at least until they are dismayed by the settlement. At a minimum, few defendants are likely to announce a settlement just before the repose period expires.

Conversely, the announcement of a settlement may also lead some institutional investors to wish to rejoin the class (in order to economize on the costs of individual litigation and avoid the risk of an adverse judgment). Questions may arise about their ability to do so after the statute of repose has expired. Some defense counsel are even arguing that a class may not be certified after the statute of repose has expired, notwithstanding that the action was filed on a timely basis. At present, this seems an extreme interpretation of CalPERS. One recent decision interpreting CalPERS cuts both ways. In Pasternack v. Schrader, 2017 U.S. App. LEXIS 12513 (2d Cir. July 13, 2017), the Second Circuit ruled that a plaintiff who filed a motion to amend within the limitations period did so on a timely basis, even though the ruling granting the motion came afterwards. The panel said that “for purposes of a statute of repose, when a plaintiff moves for leave to amend to add claims within the limitations period and attaches a proposed amended complaint to the motion, the claims are timely.” Although not precisely on point, this language suggests that if class certification is sought before the statute of repose expires, the motion need not be ruled upon before the expiration of the repose period.

The gray area under Pasternack, however, would arise when the class action is filed on a timely basis within the repose period, but no motion to certify a class is filed until after the expiration of that period. Defendants were, of course, on notice that a class action would be sought, but no motion to certify was filed, so as to come within the Pasternack formula. Such a case will likely soon arise because plaintiffs generally prefer to defer class certification until a settlement is reached in order to pass the considerable costs of notifying class members onto the settling defendants. However, if there is no settlement in prospect as the statute of repose's expiration point approaches, plaintiff's counsel will face a difficult choice: whether to bear these costs, themselves and file the certification motion, or to wait and argue that defendants had full knowledge that a class action was being sought. We express no view on how a court should rule here.

C. Statute of Limitations for SEC Disgorgement

In a decision that surprised no one, the Supreme Court unanimously held in Kokesh v. Securities and Exchange Commission¹² that the five year limitations period for SEC enforcement proceedings seeking a “civil fine, penalty, or forfeiture” also applies to disgorgement sought by the SEC. The Court reasoned that disgorgement amounts to a penalty because (1) the SEC uses that remedy to redress harm to the public and to deter securities law violations, and (2) its primary purpose was not compensation to investors. In a footnote that may overshadow the decision, the Court suggested (or at least hinted) that authority to order disgorgement in SEC proceedings may be subject to constitutional challenge.¹³ Such a challenge could place in jeopardy the contemporary system of administrative enforcement, which most administrative agencies—state and federal—utilize.

D. SLUSA and Federal Securities Class Actions in State Court

¹² 137 S. Ct. 1635 (2017).

¹³ Id at 1642 n. 3. In pertinent part, this footnote stated: “Nothing in this opinion should be interpreted as an opinion on whether courts possess authority to order disgorgement in SEC administrative proceedings or on whether courts have properly applied disgorgement principles in this context.” This possible challenge could be based on a claimed right to a jury trial or on other constitutional arguments that challenge the authority of administrative agencies generally.

Following the passage of the Private Securities Litigation Reform Act (“PSLRA”) in 1995, securities cases migrated for a time to state court (especially in California), and Congress responded by enacting the Securities Litigation Uniform Standards Act in 1998, which authorized defendants to remove to federal court securities class actions filed in state court (and certain multi-party consolidated actions). But the Securities Act of 1933 (unlike the Securities Exchange Act of 1934) always provided for concurrent jurisdiction in state and federal court; hence, cases alleging violations of Sections 11 or 12(a)(2) of the 1933 Act could arguably still be filed in state court. With respect to these federal causes of action, the language of SLUSA was somewhat ambiguous, as it provided for concurrent jurisdiction “except as provided in Section 77 of this title with respect to covered class actions.”¹⁴

The meaning of this provision has divided the lower federal courts, with district courts in the Second, Third, Fourth, Fifth and Tenth Circuits holding that SLUSA gives federal courts exclusive jurisdiction and denying remand to state courts when defendants removed such a Securities Act action, while courts in the First, Seventh, Ninth and Eleventh Circuit have held the reverse and remanded. Also, the California courts have supported concurrent jurisdiction.¹⁵ Recently, Securities Act filings in California state courts have soared, rising from only six class actions in total between 1998 and 2011 to 18 in 2016 alone.

Now, the Supreme Court has decided to resolve this division and granted cert this June in Cyan, Inc. v. Beaver County Employees Retirement Fund, 2017 U.S. LEXIS 4269 (June 27, 2017). The Court did so at the recommendation of the Acting Solicitor General, who still maintained that SLUSA does not preempt state court concurrent jurisdiction over Securities Act claims (but did agree that the instant case in Cyan could be removed to federal court). This seems a curious distinction, and it will make for a three-sided debate when the case reaches the Supreme Court.

Prediction: At least a 5-4 decision favoring the removability of such claims to federal court.

¹⁴ See 15. U.S.C. §77(v)(a).

¹⁵ See Luther v. Countrywide Fin. Corp., 195 Cal. App. 4th 789 (2011).

E. When Are Omissions of Information Actionable Under Rule 10b-5

In Leidos v. Indiana Public Retirement System,¹⁶ the Supreme Court has granted certiorari to decide this Term whether the failure to disclose information required to be disclosed by Item 303 of SEC Regulation S-K is actionable under Rule 10b-5.¹⁷ Although this is not a pure “class action” issue, it is likely to influence much class action litigation under the securities laws.

Item 303 (“Management’s discussion and analysis of financial condition and results of operations”) requires an issuer to identify and disclose both in registration statements and in periodic reports filed under the Securities Exchange Act of 1934 certain “known trends or any known demands, commitments, events or uncertainties” that are likely to affect the issuer’s liquidity or results of operations. In effect, the provision makes some forecasting mandatory. Item 303 is broad-reaching, and responses to it are much studied by the securities analysts following a company.

The plaintiffs in Leidos alleged that the company’s failure to disclose potential legal and business consequences of a kickback scheme involving a significant contract was an actionable omission under Rule 10b-5. Defendants responded that silence is not actionable, absent a duty to disclose, for purposes of Rule 10b-5.¹⁸ That response frames the largest issue in this case: Does an SEC instruction (such as Item 303) create a “duty to disclose” that makes the omission actionable (at least if scienter is also present)? If it does not, then the question arises: are issuers free to ignore the SEC’s instructions in Regulation S-K? Much will hang on the answer the Supreme Court gives to these questions. To date, the Second and Ninth Circuits have disagreed.¹⁹

¹⁶ 137 S. Ct. 1395 (May 27, 2017).

¹⁷ Regulation S-K (“Standard Instructions for Filing Forms Under Securities Act of 1933, Securities Exchange Act of 1934, and Energy Policy and Conservation Act of 1975”) can be found at 17 CFR §229.

¹⁸ This is, of course, a paraphrase of Basic, Inc. v. Levinson, 485 U.S. 224, 239 n. 17 (1988).

¹⁹ Compare Indiana Public Retirement System v. Sale, Inc., 818 F. 3d 85, 94-5 (2d Cir. 2016) and In re NVIDIA Securities Litigation, 768 F. 3d 1056 (9th Cir. 2014).

F. Predominance

In the past, predominance was seldom an issue in the certification of securities class actions. If a security traded in an “efficient” market, it qualified for the presumption of reliance announced by the Court in Basic, Inc. v. Levinson.²⁰ The class was presumed to have relied on the accuracy of the stock’s price and that that price incorporated all available material information (true and false) about the security.

More recently, however, “individual” issues have arisen that can cause a putative securities class action to flunk the predominance standard of Rule 23(b)(3). The best example is provided by Petrobas Sec. Univs. Superannuation Scheme Ltd. v. Petrobas Brasileiro S.A. Petrobas,²¹ where the Second Circuit reversed Judge Rakoff’s certification of two classes of equity and debt purchasers of Petrobas, the multinational oil and gas company headquartered in Brazil.²² Under Morrison v. National Australia Bank, Ltd.,²³ Rule 10b-5 only applies to “domestic” transactions (i.e., purchases and sales of the securities in the United States). Judge Rakoff had carefully limited his certification to purchasers “in domestic transactions,” but had deferred this inquiry about “domesticity” until the claims administration stage. Because Petrobas’s debt securities did not trade on a domestic exchange, the Second Circuit panel found that this required the district court to “assess each class member’s over-the-counter transactions for markers of domesticity under Morrison,”²⁴ and it accepted defendant’s assertion that “particularly in light of concerns over the availability and context of the necessary transaction records,” “domesticity” was a necessarily “individual” issue that precluded the predominance of common issues for purposes of Rule 23(b)(3).

What makes a securities transaction “domestic”? Under prior Second Circuit law, when securities are not traded on a domestic exchange, the transaction is considered “domestic” if (1) irrevocable liability

²⁰ 488 U.S. 224 (1988).

²¹ 2017 U.S. App. LEXIS 12219 (2d Cir July 7, 2017).

²² For the lower court’s decision, see In re Petrobas Sec. Litig., 312 F.R.D. 354 (S.D.N.Y. 2016).

²³ 561 U.S. 247 (2010).

²⁴ 2017 U.S. App. LEXIS at * 3

is incurred in the United States or (2) title passes within the United States.”²⁵ This is obviously a fact sensitive inquiry.

To determine if “domesticity” was an individual issue, the Second Circuit then relied on the Supreme Court’s 2016 decision in Tyson Foods, Inc. v. Bouaphakeo²⁶:

“An individual question is one where ‘members of a proposed class will need to present evidence that varies from member to member,’ while a common question is one where ‘the same evidence will suffice for each member to make a prima facie showing or the issue is susceptible to generalized class-wide proof.’”²⁷

On this basis, it found the District Court’s failure to determine whether the domesticity of the note purchases was “susceptible to generalized class-wide proof” amounted to an “error of law.”²⁸ Still, although the Second Circuit panel vacated the certification of the class, it remanded to the District Court to determine if some portion of the class could still be certified if generalized, class-wide evidence could establish the “domesticity” of the class’s note purchases. This seems difficult, but not clearly impossible.

In all likelihood, Petrobas will not much complicate securities class actions involving stock listed on a U.S. exchange, but where the stock or debt of an international company trades over-the-counter, certification may be difficult unless “generalized, class-wide evidence” can establish that the purchase or sale occurred within the United States.

G. Reliance and the “Fraud-On-The-Market” Doctrine

In Halliburton Co. v. Erica P. John Fund, Inc., (“Halliburton II”),²⁹ the Supreme Court re-affirmed the “fraud-on-the-market” doctrine that it had first announced in 1988 in Basic v. Levinson, but added a new twist: “defendants must be afforded an opportunity...to defeat the presumption through

²⁵ See Absolute Activist Value Mutual Fund Ltd. v. Ficeto, 677 F. 3d 60, 67 (2d Cir 2012).

²⁶ 136 S. Ct. 1036 (2016).

²⁷ 136 S. Ct. at 1045.

²⁸ 2017 U.S. App. LEXIS 12219 at *35

²⁹ 134 S. Ct. 2398 (2014).

evidence that [the] alleged misrepresentation did not actually affect the market price of the stock.”³⁰ As a result, plaintiffs must first establish market efficiency as a general matter to be entitled to the Basic presumption, but then defendants are entitled to rebut that presumption by showing a lack of “price impact,” with respect to specific disclosures.

For decades, plaintiffs have sought to establish market efficiency by reference to what are known as the “Cammer factors,”³¹ which consist of some 5 or 8 factors (depending on the Circuit). All but one of the Cammer factors utilize indirect indicia of market efficiency (e.g., trading volume, market capitalization, analyst coverage, multiple market makers). But the fifth Cammer factor looks to direct evidence, consisting of “empirical facts showing a cause and effect relationship between unexpected corporate events or financial releases and an immediate response in the stock price.” This is typically shown through event studies.³²

Over the years, courts seem to have applied the Cammer factors somewhat mechanically, and a NERA study has found that courts seemingly just count the factors, certifying the class if there are more positive factors than negative ones. Nonetheless, defense counsel regularly (and understandably) ask courts to focus on the fifth Cammer factor: did the stock price move in the right direction, particularly on corrective disclosure? If it did not, they argue that the evidence from “indirect” Cammer factors should not overcome this critical direct evidence.

This issue is at center stage in two recent Second Circuit cases, one decided and one still pending. In the Petrobas case,³³ the defendants asserted that the District Court (Judge Rakoff) had held that the plaintiffs were entitled to the Basic presumption based solely on the “indirect evidence” of market efficiency offered by the plaintiffs. This, defendants asserted, was insufficient. But the Second Circuit

³⁰ Halliburton II, 134 S. Ct. at 2417.

³¹ See Cammer v. Bloom, 711 F. Supp 1264, 1286-87 (D. N.J. 1989); see also Krogman v. Sterritt, 202 F.R.D. 467 (N.D. Texas 2001).

³² See Halliburton II, 134 S. Ct. at 2415.

³³ Petrobas Sec. Univs. Superannuation Scheme Ltd. v. Petroleo. Brasileiro S.A. Petrobas, 2017 U.S. App LEXIS 12219 (2d Cir. July 7, 2017).

panel replied that defendants’ “argument mischaracterized the district court’s analysis,”³⁴ because the district court did engage, it said, in an “involved analysis” of Plaintiff’s empirical evidence on the fifth factor.³⁵ Accordingly, the Second Circuit affirmed the District Court’s finding that the fifth Cammer factor was satisfied, and added that it “therefore decline[d] to reach the Petrobas defendant’s legal question—whether plaintiffs may satisfy the Basic presumption without any direct evidence of price impact...”³⁶

That would seemingly leave open for another day the question of “whether plaintiffs may satisfy the Basic presumption without any direct evidence of price impact.” But other statements in the Circuit Court’s opinion in Petrobas make this less certain. The “quality” of the evidence relied upon by the District Court was also disputed, and here the Second Circuit panel took a deferential approach, finding that Judge Rakoff’s findings fell “within the range of permissible decisions.”³⁷ More generally, the panel approved Judge Rakoff’s “holistic” approach that blended direct and indirect evidence. Finally, the Second Circuit rejected defendant’s insistence that the fifth Cammer factor had to be found “based on directional empirical evidence alone” as “attempting to re-label a sufficient condition as a necessary one.”³⁸

Although this may imply that, after Petrobas, the fifth factor will not be obligatory (but prudence still suggests that some evidence as to it should be presented by plaintiffs), other decisions are pending in two cases that have been argued before the Second Circuit on Rule 23(f) appeals: (1) Strougo v. Barclays PLC,³⁹ and (2) Arkansas Teachers’ Retirement System v. Goldman Sachs Group, Inc.,⁴⁰ In these cases, the application of the Cammer factors are again at issue, but at least equal attention is focused on Rule 301 of the Federal Rules of Evidence, which seemingly places the burden of production on defendants,

³⁴ 2017 U.S. App. LEXIS 12219 at *48.

³⁵ *Id.*

³⁶ *Id.* at *49.

³⁷ *Id.* at *51.

³⁸ *Id.* at *52.

³⁹ 312 F.R.D. 307, 327 (S.D.N.Y. 2016)(refusing to apply FRE 301 burden shifting). This case was argued before the Second Circuit in late 2016 and may thus be the first to be decided.

⁴⁰ 2015 WL 5613150 (S.D.N.Y. Sept 24, 2015). For the decision granting leave to appeal under Rule 23(f), see 2016 U.S. App. 23694 (2d Cir. January 26, 2016).

but the burden of persuasion on plaintiffs. From defendants' perspective, this could be a game changer for securities litigation if the Second Circuit adopted this interpretation of who has the burden of persuasion on rebutting price impact. Plaintiffs disagree as to the significance of Rule 301, noting that the burden of persuasion really matters only when the evidence is in equipoise.

The Goldman Sachs case (and other cases) will also likely test what is known as "price maintenance" theory. In the view of defendants, there should both be a positive stock market reaction following the allegedly false disclosure and a negative response after the corrective disclosure. Plaintiffs argue in response that the fraud may simply maintain the inflated price of the stock (and thus there need be no positive bump in the stock price. This theory seemed to have been approved by the Second Circuit in the related context of loss causation last year in its Vivendi decision.⁴¹ Still, one decision in the 8th Circuit may have recently taken a different view.⁴² In any event, in an important decision, Judge Easterbrook gave an incisive example of why a simple positive and negative ("up and down") price movement may not happen and why it should not be required. Suppose, he hypothesized, that the market expects the company to announce a \$50 million loss, and it instead announces a \$100 million loss, but its real loss was \$200 million.⁴³ On the false and understated announcement, the market price will go down, not up, and on the corrective disclosure, it will presumably go down more. Hence, the "up and down" price pattern is far from inevitable or logical.

H. Confidential Witnesses in Securities Litigation

Because of the uniquely high pleading standards imposed by the PSLRA in securities litigation, which require the plaintiff to plead facts giving rise to a "strong inference" of scienter,⁴⁴ plaintiff's counsel have responded by pleading statements made by unidentified "confidential witnesses." The Circuits are divided in the weight they will give to such pleadings, with the Seventh Circuit holding that

⁴¹ In re Vivendi S.A. Sec. Litig., 838 F. 3d 223 (2d Cir. 2016).

⁴² See IBEN Local 98 Pension Fund v. Best Buy Co., 818 F. 3d 775 (8th Cir. 2016).

⁴³ Schleicher v. Wendt, 618 F. 3d 679, 684 (7th Cir. 2010).

⁴⁴ See Section 21D(b)(2) of the Securities Exchange Act of 1934, 15 U.S.C. §78u-4.

the statements of confidential witnesses should be “substantially discounted”⁴⁵ while the Second and Third Circuits permit the use of confidential witnesses “provided they are described with sufficient particularity to support the probability that a person in the position occupied by the source would possess the information.”⁴⁶

Still, once one goes behind the formal doctrine and looks at the facts of these cases, there seem to be some fact patterns that trouble (and sometimes shock) judges across all these Circuits. Here, it is useful to begin with probably the best known of these decisions: Judge Posner’s 2013 opinion in the Boeing litigation.⁴⁷ There, the issue was whether senior executives at Boeing were already aware of certain stress problems that had developed in the wings of Boeing’s new “Dreamliner” aircraft at the time they announced (incorrectly) that there would be no delay in its initial flight test. The District Court had initially dismissed the complaint for failure to plead facts giving rise to a strong inference of scienter, but had allowed plaintiffs to file an Amended Complaint. The district judge then reversed her initial decision when the Amended Complaint pled that a confidential witness, described as a Boeing “chief engineer” who had worked on wing-stress tests on the Dreamliner, had seen “internal contemporaneous communications regarding the specific results of the tests and copies of internal communications to Boeing’s senior executives” informing [them] that “the tests had failed and a delay was likely.”⁴⁸

This seemed like a “smoking gun,” but it had no basis in fact. The “confidential witness” had not worked for Boeing, but only for a contractor performing low-level engineering work on a different model airplane, and had never been shown the complaint. Nor did the witness have access to Boeing’s internal data. Finally, the witness denied most of the statements attributed to him. Based on evidence to this effect, defendants convinced the trial court to reconsider her earlier denial of the motion to dismiss, and the court dismissed the complaint with prejudice.

⁴⁵ City of Livonia Emps. Ret. System & Local 295/Local 831 v. Boeing Co., 711 F. 3d 754 (7th Cir. 2013).

⁴⁶ Novak v. Kasaks, 216 F. 3d 300, 314 (2d Cir. 2000); Cal. Pub. Employees’ Ret. Sys. v. Chubb Corp., 394 F. 3d 126 (3d Cir. 2004).

⁴⁷ See City of Livonia Emps. Ret. System v. Boeing Co., *supra* note 39.

⁴⁸ 711 F. 3d at 759-761.

What had gone wrong? In a story that has occurred repeatedly, the confidential witness had been interviewed by two investigators, first in a phone call with one, and then in a two hour interview with the second. None of the plaintiff's attorneys had met the witness until after the second amended complaint had been filed; no tape recording was taken at the interview, and each investigator was alone with the witness and had no corroborating witness as to what was said.

On appeal, to the Seventh Circuit, the plaintiff's challenged the ability of the trial court to make findings on disputed facts on a motion to dismiss, but Judge Posner found that because the plaintiffs had "abandoned" "their sole confidential source"—without whom the case had earlier been dismissed—there was nothing remaining in dispute.⁴⁹ The Seventh Circuit also insisted that Rule 11 sanctions be imposed, and the District Court did so.

Not surprisingly, in a number of cases, defendants have been able to identify and interview a confidential witness for plaintiffs and have filed the witness's affidavit, which denies that the witness ever said what the complaint alleged he said, with their motion to dismiss. But this presents a procedural challenge for the district court: How is it to resolve disputed facts on a motion to dismiss when it is normally expected at this stage to accept all well-pleaded facts? The one decision that provides a clear answer is Campo v. Sears Holding Corp.⁵⁰ There, the district court noted that plaintiff's complaint was thin and hinged on statements by confidential witnesses.⁵¹ Although it denied defendant's motion to dismiss, it did so without prejudice and ordered a limited number of depositions of the confidential witnesses. Finding ultimately that these witnesses' statements at these depositions did not corroborate the statements attributed to them in the complaint, the court dismissed the complaint. On appeal, the Second Circuit affirmed, noting that the "anonymity of these sources of plaintiff's factual allegations concerning scienter frustrates [Tellabs] requirement that a court weigh competing inferences."⁵² Accordingly, the

⁴⁹ Id at 761.

⁵⁰ 635 F. Supp 2d 323 (S.D.N.Y. 2009), aff'd 371 F. App'x 212, 216 n.4 (2d Cir. 2010).

⁵¹ 635 F. Supp. 2d at 334-336

⁵² See Tellabs, Inc. v. Makor Issues & Rights, Ltd., 554 U.S. 308, 324 (2007) ("a reasonable person would deem the inference of scienter cogent and at least as compelling as any opposing inference one could draw from the facts alleged.")

Second Circuit said, “the district court’s use of the confidential witnesses’ [deposition] testimony to test the good faith basis of plaintiffs’ compliance with Tellabs was permissible.”⁵³

This decision will surprise orthodox proceduralists because it implies that Tellabs reframes the motion to dismiss for securities law cases, converting it into a comparison of competing inferences at which some discovery may be permitted. Effectively, the motion to dismiss begins to approach a mini-summary judgment motion. How other Circuits will respond to Campo remains to be seen.

Probably the most interesting and revealing District Court decision on confidential witnesses is Judge Engelmayer’s opinion in In re Millennial Media, Inc. Securities Litigation,⁵⁴ because he there undertook to set forth ethical best practices to be satisfied by plaintiff’s attorneys in connection with their use of confidential witnesses. In the Millennial case, plaintiff’s complaint attributed information to some eleven confidential witnesses. Then, one confidential witness (CW-4) informed plaintiffs that he did not wish to be quoted, and plaintiffs sought permission from the Court to file a “Supplemental Amended Complaint” that would delete all reference to CW-4. Concerned whether CW-4 had also disputed the statements attributed to him and whether plaintiffs had followed appropriate practices in dealing with confidential witnesses, the Court directed that (1) a sworn affidavit be filed by plaintiffs, signed by a “personally knowledgeable attorney explaining with specificity” the circumstances by which CW-4’s statements were included in the complaint, and (2) a sworn affidavit from CW-4 recounting his version of these events. When these affidavits were filed, it appeared that CW-4 had only been interviewed once, telephonically, by an investigator, had never been told that he would be quoted, had not been shown the complaint before it was filed, and had disputed the accuracy of several of the statements in the complaint attributed to him. Defendants then filed documents indicating that CWs 5, 8, and 11 also objected to being quoted, and some disputed the accuracy of their statements. Eventually, after further submissions mandated by the Court, the Court found that plaintiff’s counsel had never spoken to 10 of the 11 persons

⁵³ See 371 F. Appendix 212, 216 n. 4. The Court justified this investigation into “good faith” based on Rule 11’s requirement “that there be a good faith basis for the factual and legal contentions contained in a pleading...” Id.

⁵⁴ 2015 BL 169, 2015 U.S. Dist. LEXIS 69534 (S.D.N.Y. May 29, 2015), 14 Civ. 7923 (PAE).

identified as CWs; none of the 11 knew that they were to be quoted; four of the 11 (CWs 4, 5, 8, and 11) had asked to be removed from the Complaint, and at least four claimed to have either been misquoted or misleadingly quoted.

At this point, plaintiffs filed a motion for voluntary dismissal of the action, to which defendants consented. Finding these practices “unsettling” and “problematic,” the Court indicated that, even if these practices were industry-wide (as plaintiff’s counsel asserted), it found them unacceptable for two reasons: (1) the potential for inaccuracy, and (2) the unfairness to such witnesses. The Court then added that plaintiff’s counsel failure “to confirm the quotes of a witness on whom counsel purposes to rely in a public filing sits at best uneasily alongside Federal Rule of Civil Procedure 11.”⁵⁵

The Court make clear that the use of an investigator to conduct the initial interview was entirely appropriate, but, it added, Rule 11’s requirement of an “inquiry reasonable under the circumstances...demands more.” The Court’s bottom line was that it expected “counsel before filing the Complaint, to attempt to confirm with the witness the statements that counsel proposes to attribute to him and to assure that the Complaint is presenting these statements in fair context.”⁵⁶ “Basic decency,” it added, requires the same. It concluded:

“[C]ounsel here treated these people shabbily. The Court’s hope and expectation is that, in future cases, counsel will aspire to do better.”⁵⁷

There is new interest on the Federal Rules Committee (and elsewhere) in attempting to develop “best practices” for certain forms of litigation, and the use of confidential witnesses may be one of the first areas where such “best practices” are specified. Millennial Media could prove to be the model.

⁵⁵ 2015 U.S. Dist. LEXIS 69534 at *32-*33.

⁵⁶ Id at *34.

⁵⁷ Id at *44.

II. Ascertainability

“Ascertainability” continues to be one of the most controversial and fluctuating doctrinal developments in class action certification. The requirement is not found in the Rule itself, but instead is a gloss on the requirements of a class definition (found in Rule 23(c)(1)(B)) and of notice (found in 23(c)(2)). If the class must be defined and given notice, then class members must be able to be ascertained – that is, found so that they can be given notice.

Currently the landscape with respect to ascertainability splits the Circuits three ways. The Second, Fifth, Seventh and Ninth Circuits hold that plaintiffs need to show that the class is defined clearly and by objective criteria but need not show that finding each class member is administratively feasible at the class certification stage. In re Petrobras Sec., 862 F.3d 250, 257 (2d Cir. 2017)(administrative feasibility not a requirement at the class certification stage); In re Deepwater Horizon, 739 F.3d 790, 811 (5th Cir. 2014) (whether class members were actually injured is not a question for class certification but rather proof at the litigation stage); Mullins v. Direct Digital, LLC, 795 F.3d 654, 657 (7th Cir. 2015), cert. denied, 136 S. Ct. 1161, 194 L. Ed. 2d 175 (2016) (“a class must be defined clearly” and “membership be defined by objective criteria” but administrative feasibility is not required); Briseno v. ConAgra Foods, Inc., 844 F.3d 1121, 1123 (9th Cir. 2017) (stating that Rule 23 imposes no separate “administrative feasibility” requirement).

On the opposite end of the spectrum is “heightened ascertainability,” which requires that at the class certification stage the plaintiff demonstrate that there is an administratively feasible way to objectively identify class members. An affidavit from class members, standing alone, will not suffice. The Third Circuit falls into this category, Carrera v. Bayer Corp., 727 F.3d 300 (3rd Cir. 2013), and possibly the Sixth Circuit. How much evidence is needed to establish heightened ascertainability is a question that remains hotly disputed in the Third Circuit, which has reversed at least two district court decisions applying the requirement too harshly. Byrd v. Aaron's Inc., 784 F.3d 154, 171 (3d Cir. 2015), as amended

(Apr. 28, 2015); City Select Auto Sales, Inc. v. BMW of North America, -- F.3d -- (3d. Cir., August 16, 2017).

In between these two, some courts hold that plaintiff must show that they will be able to identify each injured class member, but will permit affidavits or other, relatively easy, methods to obtain proof of membership to be used to comply with this requirement. Courts that fall into this category are the Fourth, Sixth (although they may be moving towards a more rigorous standard), Eleventh, and Eighth Circuits. EQT Prod. Co. v. Adair, 764 F.3d 347, 359 (4th Cir. 2014); Rikos v. Procter & Gamble Co., 799 F.3d 497, 527 (6th Cir. 2015), cert. denied, 136 S. Ct. 1493, 194 L. Ed. 2d 597 (2016); Karhu v. Vital Pharm., Inc., 621 F. App'x 945, 948 (11th Cir. 2015); Sandusky Wellness Ctr., LLC v. Medtox Sci., Inc., 821 F.3d 992, 998 (8th Cir. 2016) (TCPA class ascertainable where list of fax numbers was available). But see Sandusky Wellness Ctr., LLC v. ASD Specialty Healthcare, Inc., No. 16-3741, 2017 WL 2953039 (6th Cir. July 11, 2017) (affidavits insufficient proof of class membership because the events occurred seven years earlier).

The remaining circuits have not addressed the ascertainability requirement.⁵⁸

There are two types of problems identifying class members that can fall under the ascertainability analysis. The first is the situation where the class members cannot be found. This is a problem of identity and might surface when the class are secondary purchasers of a retail product (such as groceries) suing a manufacturer. In such cases, if the retailer does not have records of purchases (such as through loyalty cards) then the consumers cannot be found, and defendants argue that even if class members come forward they will not have retained receipts and thus be unable to prove their purchase other than by sworn affidavit. This was the problem addressed in Carrera v. Bayer Corp., 727 F.3d 300 (3rd Cir. 2013), in which the Third Circuit articulated what remains the strongest version of the requirement – what some courts have called “heightened ascertainability.” Carrera involved allegations of deceptive advertising in

⁵⁸ In the Fourth Circuit, the term was used but the analysis was a predominance analysis rather than ascertainability. EQT Prod. Co. v. Adair, 764 F.3d 347, 359 (4th Cir. 2014). This case is discussed below.

the sale of nutritional supplements. Since there are often no records of such sales (people purchase them from sellers such as CVS or Walgreens in cash), there was no method for the court to identify each class member, and therefore the class could not be certified. *Id.* at 308. Notably, in Byrd v. Aaron's Inc., 784 F.3d 154, 171 (3d Cir. 2015), as amended (Apr. 28, 2015), the Third Circuit permitted a class to go forward over the defendants' objections on ascertainability grounds so long as the plaintiff was not relying on "unverified affidavits." *Id.* Proof of class membership could come later, the Court explained, and be contested by the defendant at that time. Similarly, in City Select Auto Sales, Inc. v. BMW of North America, -- F.3d -- (3d Cir., August 16, 2017), a junk fax case under the TCPA, the Third Circuit held that affidavits, combined with a database that was overinclusive, could suffice for ascertainability purposes. *Id.* at *5 ("Plaintiff need not, at the class certification stage, demonstrate that a single record, or set of records, conclusively establishes class membership."). In each of these cases, one of the panel dissented vigorously (Judge Rendell dissented in Byrd, Judge Fuentes in City Select), arguing that the Third Circuit should follow those Circuits that reject ascertainability as a certification requirement.

A second problem in identifying class members occurs when the class members are known – that is, their names and addresses are available, but not all the class members suffered the harm and the difficulty lies in separating the injured from the uninjured. This second problem is a problem of proof and it can sometimes appear to overlap with standing requirements. This type of identification issue was the problem addressed very recently in Sandusky Wellness Ctr., LLC v. ASD Specialty Healthcare, Inc., No. 16-3741, 2017 WL 2953039 (6th Cir. July 11, 2017). In that case the class representative sued under the Telephone Consumer Protection Act (TCPA) alleging that they were sent junk faxes in violation of the law. The problem identified by the defendant was that some of the class members had consented to receipt of the fax, a defense under the law. Other class members did not retain the fax, and thus could not prove that the defendant had failed to include certain language required by the law. By the time the suit was being litigated, it had been seven years since the faxes were sent. The Sixth Circuit expressed mistrust of class members, stating that "7-year-old, self-serving statements was not an 'administratively

feasible’ way to ascertain class membership.” Id. at 8. But it noted that if the case had been filed earlier, there might have been better solutions to the problem. Id. at 11. The panel in that case also noted its concerns about TCPA cases being a kind of “blackmail” cause of action which may have driven the analysis. Id. at 2 (stating that the TCPA junk fax rule opens businesses up to “vast liability”). Contrary precedent in the Sixth Circuit indicates that the issue of ascertainability is still unsettled there. See Rikos v. Procter & Gamble Co., 799 F.3d 497, 527 (6th Cir. 2015), cert. denied, 136 S. Ct. 1493, 194 L. Ed. 2d 597 (2016) (finding ascertainability requirement met in consumer suit when purchasers might be identified by online sales). While the two cases can be distinguished, it is also likely that the court’s perception of the social value of the overall regulatory scheme imposed by the statute in question influences its application of this requirement. In the Third Circuit, both Byrd and City Select are cases in which there was an overinclusive list of class members, presenting a problem of separating the injured from the uninjured, rather than a problem identifying class members altogether.

It is important to distinguish the problem of identifying class members from that of separating the injured from the uninjured because these two problems can have different solutions. At least one judge has suggested that the problem of separating the injured from the uninjured may be solved by sampling class members. For example in Kohen v. Pacific Investment Mgmt. Co. LLC, 571 F.3d 672 (7th Cir. 2009) Judge Posner upheld certification of a class where some members might have been injured (in that case the issue was presented as one of standing rather than ascertainability), and suggested that PIMCO “depote a random sample of class members to determine how many were net gainers from the alleged manipulation and therefore were not injured, and if it turns out to be a high percentage he could urge the district court to revisit its decision to certify the class.” Kohen, 571 F.3d at 679. Such a procedure has yet to be attempted.

Further complicating matters, it is sometimes it is difficult for courts to distinguish the ascertainability from the predominance requirement, especially in cases falling under the second type of identification problem, that is, the problem of proof of membership in the class rather than the problem of

identity. In many cases, the predominance requirement actually does the analytical work that some courts are using the ascertainability requirement to do, but predominance has the benefit of being part of the Rule. The position of the Second Circuit conflicts in a way that underscores the confusion. In In re Petrobras Sec., 862 F.3d 250, 257 (2d Cir. 2017) the Second Circuit held that a class is “ascertainable if it is defined using objective criteria that establish a membership with definite boundaries” and not requiring administrative feasibility at certification). The defendant’s argument was that the class members who purchased securities in the U.S. market could not be separated from those who did not (such purchases were a predicate to liability). The Second Circuit ultimately reversed class certification on grounds of predominance rather than ascertainability, and hinted that it may be applying a higher predominance requirement in some cases. By contrast, in Brecher v. Republic of Argentina, 806 F.3d 22, 24–25 (2d Cir. 2015), the Second Circuit stated that “[a] class is ascertainable when defined by objective criteria that are administratively feasible and when identifying its members would not require a mini-hearing on the merits of each case.” (internal citations omitted).⁵⁹ This sounds an awful lot like a ruling that individual issues predominate over collective ones. Notably, the Second Circuit in Petrobras rejected the interpretation that Brecher imposed a heightened ascertainability requirement. For another example, the defendant in Webb v. Exxon Mobil Corp., 856 F.3d 1150, 1155 (8th Cir. 2017) raised ascertainability issues in a class action arising out of title to land, but the Eighth Circuit denied certification on predominance grounds because each parcel would have to have its title searched separately without addressing ascertainability. See also Sandusky, 821 F.3d 992 (8th Cir. 2016) (holding that ascertainability requirement was met but that certification was improper on predominance grounds); Sandusky Wellness Ctr., LLC v. ASD Specialty Healthcare, Inc., No. 16-3741, 2017 WL 2953039 (6th Cir. July 11, 2017) (class certification improper on both ascertainability and predominance grounds). Another example is the Fourth Circuit’s decision in EQT Prod. Co. v. Adair, 764 F.3d 347, 359 (4th Cir. 2014). There the Court

⁵⁹ Other Second Circuit cases have denied class certification on ascertainability. See Leyse v. Lifetime Entm't Servs., LLC, 679 F. App'x 44, 47 (2d Cir. 2017).

held that proof of injury was too individualized due to “complicated and individualized” process of determining ownership of land. It decided the issue on ascertainability grounds, but the problem identified is a fairly traditional and straightforward predominance question that ought to have been decided on predominance grounds.

The reason for courts to prefer considering these issues as part of the 23(b)(3) analysis rather than as a separate heightened ascertainability requirement is that the structure of the Rule permits balancing the interests of finding injured class members and alternative methods of litigation if analyzed under the 23(b)(3) prong, whereas the ascertainability requirement (which is not explicitly in the Rule) does not permit such balancing. Mullins v. Direct Digital, LLC, 795 F.3d 654, 657 (7th Cir. 2015). It is also analytically more sensible and consistent with the language of the Rule to analyze these questions under the predominance prong, even if in many cases the outcome will be the same.

In injunctive class actions, some defendants have argued that ascertainability is a barrier to certification, but these arguments have been unsuccessful. Even the two Circuits with the most stringent ascertainability requirement do not impose this requirement in (b)(2) class actions. See Cole v. City of Memphis, 839 F.3d 530, 542 (6th Cir. 2016), cert. denied sub nom. City of Memphis, Tenn. v. Cole, 137 S. Ct. 2220 (2017); Shelton v. Bledsoe, 775 F.3d 554 (3d Cir. 2015). This trend further supports the logic of considering both questions of identification and proof of injury under 23(b)(3) predominance and superiority rather than a threshold “ascertainability” requirement.

Finally, in keeping with its general approach of treating class certification differently if it is for settlement only, the Third Circuit has held that ascertainability is not a barrier to settlement. Landsman & Funk, P.C. v. Skinder-Strauss Assocs., 639 F. App'x 880, 883 (3d Cir. 2016). This approach is difficult to square with the Supreme Court’s statement that all the rule requirements except manageability must be met for settlement class action certification. Amchem Prods v. Windsor, 521 U.S. 591 (1997).

The defendant in Briseno v. ConAgra Foods has petitioned the Supreme Court for certiorari on the ascertainability question. If the Court grants cert then it will be a difficult case for the textualists on the Court, who tend to be critical of class actions and are likely to want to uphold an ascertainability requirement even though it is not found in the Rule.

III. Justiciability

A. Standing

Article III requires an “injury-in-fact,”— an actual and concrete “invasion of a legally protected interest.” Lujan v. Defenders of Wildlife, 504 U.S. 555, 561 (1992). In Spokeo, Inc. v. Robins, 136 S. Ct. 1540, 1548 (2016), as revised (May 24, 2016) the Supreme Court addressed the question of standing in cases involving statutory privacy claims, which are often brought as class actions. Robins filed a class action lawsuit against Spokeo for publishing inaccurate information about him in violation of the Fair Credit Reporting Act. The Supreme Court held that to bring such a claim, the plaintiff must show that his injury was both concrete, “that is, it must actually exist.” Id. at 1548, and particularized. But the court below had failed to analyze whether the injury was concrete. The Court explained that while a plaintiff cannot bring an action based on a “bare procedural violation,” the “*risk* of real harm” does give rise to standing (emphasis added). Id. at 1549. This case is relevant to class actions as it was thought that it might decide what showing the plaintiffs need make in privacy and data breach class actions going forward. The Court left open to factual dispute in each case whether there is a sufficiently concrete harm. On remand, the Ninth Circuit found that the plaintiff had standing. Robins v. Spokeo, Inc., -- F.3d -- (9th Cir. Aug. 15, 2017).

The case already has resulted in courts taking a harder look at class allegations. See Strubel v. Comenity Bank, 842 F.3d 181 (2d Cir. 2016) (holding that plaintiff in putative TILA class action lacked standing to bring some claims). So far data breach cases have survived scrutiny where there are

allegations of increased risk of harm from the breach. See, e.g., In re Horizon Healthcare Servs. Inc. Data Breach Litig., 846 F.3d 625 (3d Cir. 2017).

There may be a Circuit split emerging with respect to allegations of privacy violations without additional allegations of risk of harm. Compare Perry v. Cable News Network, Inc., 854 F.3d 1336, 1340 (11th Cir. 2017) (Video Privacy Protection Act claim gives rise to standing) with Braitberg v. Charter Commc'ns, Inc., 836 F.3d 925, 930 (8th Cir. 2016) (allegations of failure to destroy personal information in violation of the Cable Communications Policy Act, without allegations of risk of harm, insufficient to establish standing). In some Circuits, even allegations of risk of harm may not be enough in data breach cases, depending on the nature of the data disclosed. For example, the Eighth Circuit held that plaintiffs may rely on a threat of future injury from disclosure to obtain standing, but that plaintiffs who alleged that their credit card information was stolen but not their social security numbers, addresses and other personal information, did not provide sufficient allegations of an injury in fact. In re SuperValu, Inc., -- F.3d --, *5 (8th Cir. Aug. 30, 2017). By contrast, the D.C. Circuit found that an allegation of a data breach is sufficient. Attias v. Carefirst, Inc., 865 F.3d 620 (D.C. Cir. 2017). As the Seventh Circuit asked (rhetorically), before Spokeo was decided: “Why else would hackers break into a ... database and steal consumers' private information? Presumably, the purpose of the hack is, sooner or later, to make fraudulent charges or assume those consumers' identities.” Remijas v. Neiman Marcus Grp., 794 F.3d 688, 693 (7th Cir. 2015).

Cases under the Fair Credit Reporting Act (FCRA) and Fair Debt Collection Practices Act (FDCPA) have not fared very well, especially where the plaintiff cannot show a risk of harm that was the type of harm the statute is trying to prevent. See, e.g., Crupar-Weinmann v. Paris Baguette Am., Inc., 861 F.3d 76 (2d Cir. 2017) (action under FCRA for printing too many digits on credit card receipt lacked standing for failure to show concrete risk of injury); Meyers v. Nicolet Rest. of De Pere, LLC, 843 F.3d 724 (7th Cir. 2016), cert. denied, 137 S. Ct. 2267 (2017) (same); Dreher v. Experian Info. Sols., Inc., 856 F.3d 337, 345 (4th Cir. 2017) (failure to provide accurate information under the FCRA insufficient to give

rise to standing where the plaintiff could show no “real world effect”); Groshek v. Time Warner Cable, Inc., No. 16-3355, 2017 WL 3260080, at *3 (7th Cir. Aug. 1, 2017) (failure to provide information under the FCRA insufficient to give rise to standing where the plaintiff did not request a corrected disclosure and information at issue did not relate to the interests that the statute was trying to protect); Lyshe v. Levy, 854 F.3d 855, 859 (6th Cir. 2017) (plaintiff alleging that the defendant misrepresented state procedural rules in discovery requests, in violation of the FDCPA, did not have standing because it was “not the type of harm the FDCPA was designed to prevent” and plaintiff conceded he was not at risk to suffer harm from the violation). Analogously, the Eleventh Circuit denied standing where a mortgagor failed to comply with state law in timely filing the mortgage, but the mortgagee waited two years to file suit and was unharmed by the delay. Nicklaw v. CitiMortgage, Inc., 855 F.3d 1265, 1267 (11th Cir. 2017). But see Sayles v. Advanced Recovery Sys., Inc., 865 F.3d 246 (5th Cir. 2017) (standing found in FDCPA case where “violation exposed [plaintiff] to a real risk of financial harm caused by an inaccurate credit rating.”)

Whether a case can survive Spokeo appears to turn on whether the plaintiff can convince the court that there is a real risk of injury and that the violation is not merely a technical violation without much consequence. The purpose of the statute in question is relevant as well. The Eleventh Circuit, for example, emphasized the purpose of the Video Privacy Protection Act, which was passed in the wake of a video rental store revealing the rental habits of Supreme Court nominee Robert Bork, in holding that the invasion of privacy is sufficient to give rise to standing under that statute without further proof of injury. Perry v. Cable News Network, Inc., 854 F.3d at 1340.

Once the named plaintiff shows that he has standing, is this sufficient for class certification or must standing be shown for each and every class member? Most Circuit courts that have considered the question have ruled that once the class representative shows that he has standing – which is clearly necessary under Article III – then the requirements of standing are met. See O’Shea v. Littleton, 414 U.S. 488, 494–495 (1974) (requiring that named plaintiff have standing). One example of this approach is

Neale v. Volvo Cars of N. Am., LLC, 794 F.3d 353 (3d Cir. 2015). That case involved allegations of defective sunroof drainage systems in Volvo cars. The defendant argued that the class representative had not carried her burden of proving that each and every class member was injured in order to have Article III standing for the class action. The Third Circuit held that all that is needed is to prove that the class representative has standing, reasoning from the history of representative actions. Relying on the “entity” view of class actions, the court reasoned that once the class representative had standing the entity created by the class certification process has standing as well. That is, once the inquiry into the class representatives standing is complete, the rest of the analysis is based only on Rule 23. Id. (“Requiring individual standing of all class members would eviscerate the representative nature of the class action. It would also fail to recognize that the certified class is treated as a legally distinct entity even though the outcome of such an action is binding on the class.”).

A court need not go so far as to adopt the entity view of the class action to see that Article III standing can be met in a class action by the class representative. This is because once the class representative is shown to have standing, if the class is well defined and the class representative is typical of that class, then the court has all it needs to proceed. That is, the court can assume that what was true for the class representative is true for the class as a whole. See, e.g., Denney v. Deutsche Bank, 443 F.3d 253 (2d Cir. 2006) (holding that the class “must be defined in such a way that anyone within it would have standing.”)

But what happens if some (but not all) of the class members are alleged by the defendant to lack an “injury-in-fact”? It continues to come up in different form as part of the ascertainability inquiry in some circuits, but less often as a standing question, at least recently. As an Article III question, the issue was addressed by the Seventh Circuit in Kohen v. Pacific Investment Mgmt. Co. LLC, 571 F.3d 672 (7th Cir. 2009). The case involved shares purchased on the Chicago futures market. The facts of the case are somewhat complicated, but the bottom line was that it was impossible to tell at the class certification stage which class members actually suffered monetary damages as a result of the defendant’s market

manipulation (and defendant argued that some may have even benefitted from it). The defendant argued that it was the plaintiff's burden to prove at the class certification stage that all the class members had suffered damages. Judge Posner rejected this argument: "as long as one member of a certified class has a plausible claim to have suffered damages, the requirement of standing is satisfied." Id. at 676. Of course at trial the plaintiffs would have to prove damages, but as the court noted if a plaintiff fails to prove damages he loses his case, the court's jurisdiction does not evaporate. Ibid. See also Lexmark International v. Static Control Components, 134 S. Ct. 1377, 1391 n. 6 (2014) (stating that "the absence of a valid (as opposed to arguable) cause of action does not implicate subject-matter jurisdiction" (citation omitted)).

When a class is alleged to include class members who are uninjured, this is a potential problem of class definition; that is, perhaps the class definition is too broad. But one must be careful, because a class definition cannot include within it elements of liability or the class may be denied certification on grounds that is a so-called "fail safe" class. See, e.g., Messner v. Northshore Univ. Syst., 669 F.3d 802, 825 (7th Cir. 2012) (explaining that a "fail safe" class "is improper because a class member either wins or, by virtue of losing, is defined out of the class and is therefore not bound by the judgment.").⁶⁰

So what is to be done as a matter of Rule 23? Judge Posner suggests that if indeed it is the case that much of the class is not entitled to damages because they gained from the defendant's market manipulation, the defendant bears the burden of proving that allegation. He suggested that PIMCO "depote a random sample of class members to determine how many were net gainers from the alleged manipulation and therefore were not injured, and if it turns out to be a high percentage he could urge the district court to revisit its decision to certify the class." Kohen, 571 F.3d at 679. So far, other courts have not taken up this suggestion and, as we have seen, will either reject or permit class certification under the ascertainability prong.

⁶⁰ Not all courts accept the "fail safe" doctrine. See, e.g., In re Rodriguez, 695 F.3d 360, 370 (5th Cir. 2012) (rejecting the doctrine).

B. Mootness

Campbell-Ewald Co. v. Gomez, 136 S. Ct. 663 (2016) posed the issue of whether defendants could pick off this class representative by offering him or her full individual relief to moot both the representative's claims and the putative class action. The court (narrowly) sided with the plaintiffs and found that an unaccepted offer to satisfy the named plaintiff's individual claim does not render the case moot or bar class certification. At the end of the Court's analysis of the issue of mootness, there appear the following two sentences:

“We need not, and do not, now decide whether this result would be different if a defendant deposits the full amount of the plaintiff's individual claim in an account payable to the plaintiff, and the court then enters judgment for the plaintiff in that amount. That question is appropriately reserved for a case in which it is not hypothetical.”⁶¹

This narrow distinction between an offer and an actual tender of payment sounds much like a concession by the majority to hold onto the vote of a Justice who was wavering (and Justice Kennedy was the swing vote in this case). Thus, we are left with a major uncertainty: Can defendants pick off the class representative if they actually tender the full amount that satisfies his claim?

Courts have taken a very rigorous approach to defendant attempts to take up the Supreme Court's invitation. A good example is Fulton Dental, LLC v. Bisco, Inc., 860 F.3d 541, 545 (7th Cir. 2017). The defendant attempted to deposit the full statutory amount due in a TCPA case with the court, which Rule 68 permits. The Seventh Circuit rejected this attempt to pick off the lead plaintiff on two grounds. First, the Court ruled that plaintiff ought to have an opportunity to contest whether the payment was a payment in full – the plaintiff here claimed that it expected an additional payment for its participation as a class representative, and thus the amount placed with the court was not a full tender. Second, the Court held that placing money with the Court was insufficient to meet the Supreme Court's invitation to tender the full amount because the money could not be withdrawn by the plaintiff at its discretion: “funds can be

⁶¹ 136 S. Ct. 663, 672.

withdrawn from the court's registry only under the control of, and with the permission of, the court....” Id. at 545. See also Conrad v. Boiron, Inc., No. 16-3656, 2017 WL 3623960, at *4 (7th Cir. Aug. 24, 2017).

The Ninth Circuit similarly rejected a defendant’s attempt to put full relief in escrow and use this to moot plaintiff’s claim, explaining: “a claim becomes moot when a plaintiff *actually receives* complete relief on that claim, not merely when that relief is offered or tendered. Where, as here, injunctive relief has been offered, and funds have been deposited in an escrow account, relief has been offered, but it has not been received.” Chen v. Allstate Ins. Co., 819 F.3d 1136, 1138 (9th Cir. 2016). See also Radha Geismann, M.D., P.C. v. ZocDoc, Inc., 850 F.3d 507, 513 (2d Cir. 2017) (Rule 68 offer followed by the district court entering judgment does not moot a case: “The result in *Campbell–Ewald* cannot be avoided simply by entering a judgment effectuating an otherwise precluded dismissal.”);⁶² Conway v. Portfolio Recovery Assocs., LLC, 840 F.3d 333, 335 (6th Cir. 2016) (“a ‘judgment that should never have been entered does not snuff out a plaintiff’s stake in the underlying litigation.’”).

One of the risks created by Campbell-Ewald is that plaintiffs would find it necessary rush to file “placeholder” class certification motions to preserve their rights before defendants could moot the case. So far, appellate courts have largely held that plaintiffs need not file placeholder motions and are entitled to a “fair opportunity” to seek certification after a case is mooted. For example, the Third Circuit held that when an injunctive claim has been mooted, the plaintiff is still entitled to a “fair opportunity” to seek class certification. Richardson v. Bledsoe, 829 F.3d 273, 283 (3d Cir. 2016). The Court explained

“Our ruling today is intended to have the salutary effect of discouraging these premature motions in favor of motions brought within a reasonable period of time and after proper factual development of the claims has occurred. This is so because a plaintiff, by waiting until it would be appropriate to seek class certification, does not run the risk of having the entire class action mooted in the interim.”

Id. at 284. See also Wilson v. Gordon, 822 F.3d 934, 951 (6th Cir. 2016)(holding that when defendant in an injunctive case attempts to moot plaintiffs’ case by correcting the problem as to that plaintiff only, this

⁶² But see Leyse v. Lifetime Entm’t Servs., LLC, 679 F. App’x 44, 48 (2d Cir. 2017). In that unpublished opinion in a TCPA case, the defendant did deposit the full amount in an account payable to the plaintiff, and the court upheld the entry of judgment and held that the case was moot. Separately, the court also held that the class could not be certified on ascertainability grounds.

will not moot the class action); Chen v. Allstate Ins. Co., 819 F.3d 1136, 1138 (9th Cir. 2016)(TCPA plaintiff can still pursue class action even if his individual claim is fully paid by the defendant); Laurens v. Volvo Cars of N. Am., LLC, 868 F.3d 622, 622 (7th Cir. 2017) (holding that “an unaccepted pre-litigation offer does not deprive a plaintiff of her day in court.”).

It is important to note that the “pick off” tactic might not be effective in some contexts—such as securities or antitrust class actions—where the class representative often holds multimillion dollar claims that would be prohibitive to settle at their full face value, but it seemed promising as a defense tactic in defective products and consumer fraud cases where the class representative usually has a small, “negative value” claim that it could not afford to pursue individually. In such a context, the defendants could easily pay off even a string of individual plaintiffs, until the plaintiff’s attorney ran out of individual clients with whom to pursue a class action.

IV. Changes to Rule 23

Changes to Rule 23 are coming after a few years of research and contemplation on the part of the Rule 23 Subcommittee. There is every indication that the Rule changes will be approved this year. The changes are unlikely to bring major changes to class action practice, but they do codify some best practices.

The most significant of the changes is probably the provision on objectors. Under the current iteration of the Rule, objectors only needed to obtain court approval to withdraw their objection, but were not required to reveal any information regarding their reasons for withdrawing their objection. Concerns have often been raised about objectors who use the delay of an appeal to pressure the plaintiffs’ counsel to pay them a substantial sum (relative to other class members) in exchange for withdrawing their objection. Some commentators were also concerned that groups of class members were bought off in this way at the expense of other class members who did not object, but more recently the concerns have largely been

about objectors using the threat of delay to extract additional payments for themselves without benefitting the whole class. To address this problem, the new Rule 23(e)(5) requires objectors to obtain court approval to be paid in connection with withdrawing their objection either at the district court or appellate level. Notably, side agreements are still not required to be disclosed, only the fact of the agreement.

The revised Rule also includes new provisions with respect to settlements. First, a “front loading” provision allows the judge to evaluate the likelihood of the settlement being approved before ordering notice of the settlement, so that two notices need not be sent out if the judge determines the settlement is not fair and equitable. In the revised language, a judge must order notice “if giving notice is justified by the parties’ showing that the court will likely be able to: **(i)** approve the proposal under Rule 23(e)(2); and **(ii)** certify the class for purposes of judgment on the proposal.” Fed. R. Civ. P. 23(e)(1)(B) (as revised). Judges were already doing this, but now this best practice is incorporated formally into the rule. Fed. R. Civ. P. 23(e)(3).

Second, the Rule will spell out the major considerations for a court to approve a settlement as fair and equitable. They are:

- (A)** the class representatives and class counsel have adequately represented the class;
- (B)** the proposal was negotiated at arm’s length;
- (C)** the relief provided for the class is adequate, taking into account:
 - (i)** the costs, risks, and delay of trial and appeal;
 - (ii)** the effectiveness of the proposed method of distributing relief to the class, including the method of processing class-member claims, if required;
 - (iii)** the terms of any proposed award of attorney’s fees, including timing of payment; and any agreement required to be identified under Rule 23(e)(3); and
 - (iv)** any agreement required to be identified under Rule 23(e)(3); and
- (D)** class members are treated equitably relative to each other.

These are not (we hope) listed in order of their importance, as the fact that class members are treated equitably is listed last rather than as the first consideration. We address the significance of some of these provisions for attorney's fees below.

Finally, the revised Rule permits notice to be electronically disseminated or by first class mail, as appropriate. This does not change the general rule that notice must be reasonably calculated to notify the class members of the pendency of the action under the circumstances, but as some judges were rejecting notice that was not first class mail (even though the prevailing rule did not require it), the revision was felt to be necessary. This could make notice considerably cheaper in cases where email notice is appropriate, but it is important to remember that for some populations web-based notice will not suffice.

V. Appeals of Class Certification Orders

Appeals from class certification orders usually fall under Rule 23(f), which permits the appellate courts to take appeals from class certification decisions at their discretion. In Microsoft Corp. v. Baker, 137 S. Ct. 1702 (2017), a plaintiff who had lost his class certification motion and was denied 23(f) review voluntarily dismissed the action and sought appellate review of the judgment as a way of forcing appellate decision on the class certification question. The Supreme Court held that this was not a "final decision" as defined by 28 U.S.C. § 1291. This holding was consistent with the Court's refusal to permit appellate review of class certification decisions in Coopers & Lybrand v. Livesay, 437 U.S. 463, 470 (1978). In Microsoft, the Court returned to the rule articulated in Coopers & Lybrand and explained that even though the class certification motion could be determinative, it was not final and therefore no appeal could be had. The exception created by 23(f), which permits appellate courts to review class certification motions at their discretion, sufficiently balanced the interest of the court system in finality with the interests of the parties in obtaining mid-suit review of certification decisions. Justice Ginsburg, writing for the Court, explained: "Respondents' voluntary-dismissal tactic, even more than the death-knell theory, invites protracted litigation and piecemeal appeals." Microsoft Corp., 137 S. Ct. at 1713.

One important aspect of the opinion is Justice Ginsburg’s focus on parity between plaintiffs and defendants. She explained that “[r]espondents’ theory permits plaintiffs only, never defendants, to force an immediate appeal of an adverse certification ruling. Yet the “class issue” may be just as important to defendants. . .” *Id.* at 1715. This is important because the “death knell” theory for interlocutory appeals was a plaintiff’s theory (that denial of certification meant a “death knell” for the class). By contrast, the move towards permitting appeals under 23(f) was driven largely by the increased perception in the 1990s that defendants faced “blackmail” if classes were certified.

Justice Ginsburg emphasized the language of the Rule itself and the “carefully calibrated” balance struck by the rule-makers. She also made heavy use of the Committee Notes, an interpretative approach that had come under fire from Justice Scalia and which may prove important if the question of whether ascertainability is a valid requirement for class certification ever comes before the Court.

Justice Thomas, joined by Justice Alito, concurred in the judgment but would have decided the case on constitutional grounds. “When the plaintiffs asked the District Court to dismiss their claims,” wrote Justice Thomas, “they consented to the judgment against them and disavowed any right to relief from Microsoft.” Microsoft Corp., 137 S. Ct. at 1717.

VI. Injunctive Class Actions

One disturbing development in 23(b)(2) class actions has been the increasing deployment of the argument that class certification is not necessary because the court’s grant of an injunction and declaratory relief as to the individual plaintiff will be binding on the defendant and inure to the benefit of the entire class. There is no necessity requirement in Rule 23 and indeed the short statement of the requirement for certifying a (b)(2) class does not admit much in the way of policy considerations as to the benefits of proceeding collectively, unlike (b)(3) which does. See Rule 23(b)(2) (“the party opposing the

class has acted or refused to act on grounds that apply generally to the class, so that final injunctive relief or corresponding declaratory relief is appropriate respecting the class as a whole”). It is hard to find in this language the requirement that courts balance whether class or individual proceedings are preferable, but some courts have stated that necessity may be considered as part of the question of whether “relief is appropriate respecting the class as a whole” which strikes one of us as an implausible reading.

In any event, it is worth asking *why* a defendant would want to fight class certification if the injunction will indeed force it to act similarly with respect to all class members. The very fact that defendant opposes the class action indicates that it will derive some benefit from proceeding individually, and that benefit is likely to be that it can treat the decision more narrowly than if it had been class wide. Thus, this is an especially worrying tool in the hands of recalcitrant defendants. For example, if the school board in Brown v. Board had been sued by Oliver Brown individually, the school could have admitted him, taught him in a separate classroom from the other students, and resisted integration. Furthermore, the class action device protects other class members who may be affected by the injunction. Newberg on Class Actions § 4.35 (“Class certification serves one central function even if an individual action [against the government] would itself achieve the class’s ends—class certification ensures that the class is adequately represented...”).

The controversial idea seems to be in the air but not coalesced. As the author of the prominent class action treatise writes: “Like Newton’s Law of Thermodynamics, for every class denial on the basis of lack of need, one is able to find a decision, or several decisions, often in the same circuit, where other courts have certified Rule 23(b)(2) classes under virtually the same circumstances.” William B. Rubenstein, Newberg on Class Actions § 4.35 (2017) (collecting cases). The Seventh Circuit entirely rejects this requirement. Brown v. Scott, 602 F.2d 791, 795 (7th Cir. 1979). But other circuits sometimes permit consideration of necessity as part of the “appropriate relief” language in 23(b)(2), holding that the class should not be certified when certification is “formality or otherwise inappropriate.” Dionne v. Bouley, 757 F.2d 1344, 1356 (1st Cir. 1985); Gayle v. Warden Monmouth Cty. Corr. Inst., 838 F.3d 297,

310 (3d Cir. 2016) (but warning that “[t]he circumstances in which classwide relief offers no further benefit, however, will be rare, and courts should exercise great caution before denying class certification on that basis.”).

VII. After the Settlement: Fees and the Distribution Process

The post-settlement context includes a range of issues and problems, some of which courts have tended to slight.

A. Attorney’s Fee Awards.

Nearest and dearest to the plaintiff’s attorney’s heart is the topic of attorney’s fees. Classically, there are two approaches: the percentage of the recovery and the lodestar (with the former being much more frequently used). Nonetheless, in July, 2017, the 10th Circuit surprised many by announcing that the “percentage of the recovery” formula could not be used in a case involving a \$52 million settlement based on underpayment of royalties on gas from oil wells.⁶³ The decision in Chieftain Royalty Co. v. Enervest Energy Institutional Fund was 2-0, as the third judge, Neil Gorsuch, moved on to a different court (we may someday learn how he would have ruled). The District Court had approved the settlement and approved a 30% fee award on the percentage of the recovery basis. Objectors took an appeal to the 10th Circuit, which reversed. The rationale for the reversal was that Oklahoma law governed and forbade the percentage of the recovery approach. This raises the always complicated issue of the application of Erie v. Tompkins⁶⁴ to arguably procedural issues. As the 10th Circuit panel saw it, Erie required it to apply Oklahoma law in diversity cases. Still, Hanna v. Plumer generally requires that the federal rules of procedure should be applied uniformly in federal court.⁶⁵ The 10th circuit saw no conflict, ruling that:

⁶³ Chieftain Royalty Co. v. Enervest Energy Institutional Fund, 2017 U.S. App. LEXIS 11801 (10th Cir. July 3, 2017)

⁶⁴ See Erie R.R. Co. v. Tompkins, 304 U.S. 64 (1938).

⁶⁵ 380 U.S. 460, 468 (1965).

“[A]t least when there is no contrary federal rule of civil procedure properly enacted under the Rules Enabling Act... the Erie doctrine requires federal courts to ‘conform as near as may be—in the absence of other considerations—to state rules may bear substantially on the question whether the litigation would come out one way in federal court and another way in state court if the federal court failed to apply a particularly rule...”⁶⁶

In short, although Rule 23 requires the court to approve the fee award in a class action, it never specifies the criteria or methodology, and here the court must look to state law. The 10th Circuit also drew a distinction between “substantive fees” and “procedural fees.” The former depend on the outcome of the case (i.e., contingent fees are one example) and must be determined under state law, while procedural fees are fees given to the court’s discretion (such as the fees for a violation of Rule 11) and are determined by federal law.

This holding will not affect attorney’s fees in cases founded on federal question jurisdiction, but courts hearing, for example, derivative actions based on diversity may be well required to look to state law in awarding attorney fees. Of course, the fact that state law controls does not imply that the percentage of recovery method is invalid under state law. Oklahoma had a special rule in this regard.⁶⁷ Other states take the percentage of the fund approach.⁶⁸

Recent empirical research on attorney’s fees has reached some provocative findings. A detailed study by Professor Brian Fitzpatrick in 2010 concluded:⁶⁹

1. Most judges do follow the percentage of recovery approach;
2. Fee awards vary widely, but both the mean and median award in this study were 25%;
3. Fee size is a declining percentage of the recovery;

⁶⁶ 2017 U.S. App. LEXIS 11801 at *3 (citing Byrd v. Blue Ridge Rural Elec. Corp., 356 U.S. 525, 5353 (1958)).

⁶⁷ See Burk v. Oklahoma City, 598 P. 2d 659 (Okla. 1979).

⁶⁸ See, e.g., Laffitte v. Robert Half Int’l Inc., 1 Cal. 5th 480, 376 P.3d 672 (2016) (holding that a percentage of the fund is the preferred method in California).

⁶⁹ Fitzpatrick, An Empirical Study of Class Action Settlements and Their Fee Awards, 7 J. Empirical Legal Studies 811 (2010).

4. Fee awards in Circuits with a high volume of securities litigation (i.e., the Second and the Ninth) were a smaller percentage of the recovery than elsewhere.

A more recent 2015 study by Professors Lynn Baker, Michael Perino and Charles Silver⁷⁰ came to similar conclusions with regard to the finding that fees are lower in federal districts that see a high volume of securities class actions, and they further found that such judges in high volume districts are significantly more likely to cut the requested fee. What explains this? Does familiarity breed contempt? Lastly, they found that lodestar cross-checks are associated with significantly higher fee awards. Their hypothesis is that lawyers use the cross-check as a justification only when they anticipate a possible fee reduction.

This evidence about inter-Circuit variation and the limited utility of the cross-check does not necessarily lead to any specific reform proposal, but Professors Baker, Perino, and Silver do advance one: the lead plaintiff should negotiate a fee when retaining class counsel and disclose it to the district court when it is asked to approve the choice of class counsel. Generally, they suggest, the court should defer to these provisions unless “clearly unreasonable.” Arguably, this is a “best practices” standard, and it is similar to practices actually followed today in the Seventh Circuit, where deference is given to fee formulas negotiated by sophisticated institutional investors.⁷¹ Nonetheless, outside the Seventh Circuit, this approach has not attracted much judicial support.

B. Holdbacks and Proposed Rule 23(e)(2)

Another important question about fee awards is when they should be paid. A number of district judges normally employ a “holdback” procedure, under which they hold back some portion of the fee

⁷⁰ Lynn Baker, Michael Perino, and Charles Silver, Is the Price Right?: An Empirical Study of Fee-Settling In Securities Class Actions, 115 Colum. L. Rev. 1371 (2015).

⁷¹ See, e.g., In re Synthroid Mktg. Litig., 264 F. 3d 712, 718-719 (7th Cir. 2001); Montgomery v. Aetna Plywood, Inc., 231 F. 3d 399, 409 (7th Cir. 2000). These cases look to the market rate, as judged by the agreements that sophisticated institutional investors reach with class counsel. This approach is sometimes called the “market-mimicking” approach, and it assumes that “ex ante” negotiation of fees is preferable to “ex post” negotiation of attorneys fees.

award (say, 50%) until the settlement has been distributed or largely distributed. They believe that this encourages expedition on the part of plaintiff's attorneys.

Recently, proposed Rule 23(e)(2) seeks to encourage the use of holdbacks. In particular, it provides that before approving a class action settlement as "fair, reasonable, and adequate," the court should consider a variety of factors, including:

"(C)(iii) the terms of any proposed award of attorney's fees, including timing of payment;..."

The proposed rule then explains in a Committee Note that:

"The proposed handling of an award of attorney's fees under Rule 23(h) ordinarily should be addressed in the parties' submission to the court. In some cases, it will be important to relate the amount of an award of attorney's fees to the expected benefit to the class. One way to address this issue is to defer some or all of the award of attorney's fees until the court is advised of the actual claims rate and results."

This use of holdbacks goes beyond using them to expedite payment to the class and sees them as a way of relating the award to the amount actually received by the class. It should not be forgotten that, in the case of securities class actions, federal law mandates that the fee award not exceed a "reasonable percentage" of the amount "actually paid to the class."⁷²

C. Smaller Claimants and Equitable Distribution

Another important topic at the "post-settlement" stage is how to reach the smaller claimant. Securities litigation typically has many large claimants (i.e., institutional investors), and today they do typically file claims and are well compensated. In part, this may be because the size of securities class actions settlements has recently increased. As they have, institutional investors have become much more interested in filing claims.

⁷² In the case of a securities class action, the Securities Exchange Act provides in Section 21D(a)(6) that the fee award (including expenses) "shall not exceed a reasonable percentage of the amount of any damages and prejudgment interest actually paid to the class." This would appear to preclude considering any ex pres recovery in determining the fee award.

But this does not imply that smaller claimants file claim forms at a similar rate. In the world of consumer class actions, the data is sparse but what exists indicates that most of the time claiming rates are very low. This high variance may be a product of the method for claiming imposed by the settlement. That is, the claims filing rate can be under 1% (and sometimes considerably lower, as some anecdotal evidence suggests that was collected in the legislative history to the proposed “Fairness in Class Actions” statute, which recently passed the House).⁷³ Alternatively, the rate may sometimes be as high as 60-70%.⁷⁴ Often, a low claiming rate may be the result of elaborate documentation requirements imposed by defendants; sometimes, it may reflect class member indifference to a small recovery, a reaction to the time involved in filling out even modest forms, or the form of notice. Generally, defendants only have a strong incentive to impose a burden on claiming when the settlement is a “claims made” or reversionary one (which settlements are increasingly uncommon). New electronic claims methods that permit class members to obtain compensation through online vendors such as Amazon or Paypal anecdotally report higher uptake rates, although there are no published studies available. More transparency here is needed, before any overall evaluation of the success of consumer class actions is possible.

In the securities class action field, there are usually repeated distributions (three or four) until the amount left in the fund is reduced to a level that is below the mailing costs of another distribution (and this balance is then distributed in a cy pres distribution to some charity). This pattern does not, however, resolve all concerns. Arguably, in securities class actions, a fundamental conflict of interest surrounds the distribution process. The lead plaintiff is, by law, a large investor with one of the largest stakes in the

⁷³ For example, in one case a declaration by a settlement claims administrator stated that the median claims rate for consumer class action settlements is .23%. See *Poertner v. The Gillette Company*, 612-CV-00803 (GAP) (Decl. of Deborah McComb, April 21, 2014, ¶ 5) (“KCC did an analysis six months ago of all consumer class action settlements that KCC administered where the notice provided to class members relied entirely on media notice rather than direct mail notice. These settlements included products such as toothpaste, children’s clothing, heating pads, gift cards, an over-the-counter medication, a snack food, a weight loss supplement and sunglasses. The claims rate in these cases ranged between .002% and 9.378%, with a median rate of .023%.”). We do not know the claiming rate when direct mail notice, email notice, or other forms of notice are used.

⁷⁴ See Brian T. Fitzpatrick & Robert C. Gilbert, *An Empirical Look at Compensation in Consumer Class Actions*, 11 N.Y.U. J.L. & Bus. 767, 787 (2015) (finding that claiming rates can be as high as 60 or even 70% when payment is automatic and claim forms are not required).

action, and it, as a practical matter, chooses class counsel, and heavily influences the choice of the Claims Administrator. Large investors have very little incentive to spend significant funds in locating small investors (with whom they would then have to share the settlement fund if they were located). I do not suggest that anyone discourages small claimants, but the zeal of large institutional investors to find small claimants with whom to share the settlement fund is not overwhelming. Admittedly, at some point, the effort to find small claimants would be disproportionate and excessive. It would be silly to spend \$1 million to convince an additional \$200,000 in small claims to file. But we are not near that point.

Proposed Rule 23(e)(2)(D) arguably addresses this tension by requiring the court to consider in evaluating the fairness of the settlement whether “the proposal treats class members equitably relative to each other.” If approved, this provision focuses the court on intra-class disparities.

What should be done? Rule 23(e)(2) suggests that the court should consider the “claims rate” in determining the fee award. Possibly also, the district court should play a stronger role in selecting and supervising the Claims Administrator. As a best practice, the District Court could ask (and be advised) as to the claims filing rates for investors at different ownership levels (e.g., over \$1 million, below \$1 million, and down to under \$10,000).

Many have proposed simplifying claims forms, using Plain English, and permitting electronic filings. More Power to such proposals! But, if there is a low rate of filing by smaller claimants (and the evidence is far from clear because there is little transparency), what we should want is twofold: First, we need greater transparency by collecting data on claim filing rates by investor size. Second, if there is a problem with low filings by smaller claimants, the simplest answer may be to offer bounties to Claims Administrators who succeed in obtaining a higher rate. For example, if less than 5% of claimants with claims under \$10,000 normally file in a consumer class action, a Claims Administrator who convinces 10% or more of such investors to file deserves a bounty (paid as part of the administrative costs of a settlement).

D. Cy Pres Recoveries

The American Law Institute has expressed skepticism about the use of cy pres recoveries, and a number of decisions have disfavored them. See American Law Institute, *Principles of Aggregate Litigation*, §3.07 (2010). Nonetheless, in Keepseagle v. Perdue, 2017 U.S. App. LEXIS 8449 (D.C. Cir. May 16, 2017), the D.C. Circuit approved a large cy pres settlement under which most of the remaining \$380 million in the compensation fund in a class action would go to a variety of non-profit organizations that provided services to Native American farmers. The litigation had had a long and tortured history, beginning in 1999 when Native American farmers sued the Department of Agriculture for discrimination in various benefit programs. The action settled for \$680 million, but it proved infeasible to distribute more than \$300 million to claimants, as few filed. A revised settlement was negotiated under the court's supervision that provided for the remainder to be distributed both to cy pres beneficiaries and to those who had received an earlier distribution. This did not satisfy some class members who wanted the entire remainder to be distributed proportionately to those who had earlier filed claims and received an initial distribution.

In the course of rejecting these claimants, the D.C. Circuit panel discussed decisions in other Circuits that had rejected cy pres distributions and found that they involved fact patterns in which the cy pres distribution was not expressly negotiated in the settlement.⁷⁵ By implication, it agreed that standardless discretion might be improper, as was the court or special master making the distribution according to its own preferences and without authorization in the settlement agreement. On its facts, Keepseagle seems hard to quarrel with for a variety of reasons. Had the cy pres provision not been approved, an extraordinary amount of money would have gone to a few members of a very large class

⁷⁵ The cases so distinguished included: In re Baby Prods. Antitrust Litig., 708 F. 3d 163, 172 (3d Cir. 2013); In re Lupton Mktg. & Sales Practices Litig., 677 F. 3d 21 (1st Cir 2012); and In re Katrina Canal Breaches Litig., 628 F. 3d 185 (5th Cir. 2010). In these cases, either the beneficiaries were completely unrelated to the purposes of the litigation or the court or magistrate had standardless discretion to pick the recipients.

(despite the efforts of the class’s own representatives to direct the funds to beneficiaries serving the class as a whole.)

E. Injunctive Relief in Consumer Class Actions

The phenomenon of “disclosure only” settlements in merger litigation was discussed previously in this memo and has been much criticized. But this form of recovery – if it can be called that – can also be found in some consumer class actions. A recent decision out of the Seventh Circuit takes aim at these practices. In re Subway Footlong Sandwich Mktg. & Sales Practices Litig., No. 16-1652, 2017 WL 3666635, at *5 (7th Cir. Aug. 25, 2017). Plaintiffs brought a class action claiming that the “foot long” subs sold by the Subway sandwich chain were not in fact twelve inches long.⁷⁶ In settlement, Subway agreed to a disclaimer about the length of its “foot-long” subs, to cap attorney’s fees at \$525,000 (that is, that it would agree to such a fee), and that each class representative should receive no more than \$1,000 for his efforts. The court approved the settlement, awarding \$520,000 in fees and \$500 to each class representative. Id. at *3. The objector appealed. In its decision to reverse and remand, the Seventh Circuit wrote:

Here, the procedures required by the settlement do not benefit the class in any meaningful way. The settlement acknowledges as much when it says that uniformity in bread length is impossible due to the natural variability of the bread-baking process. Contempt as a remedy to enforce a worthless settlement is itself worthless. Zero plus zero equals zero.⁷⁷

Little more can be said except that this exemplifies the need for constant vigilance of class action settlements and the importance of structuring attorney’s fees to provide incentives for class counsel to produce better outcomes for class members.

VIII. Arbitration

⁷⁶ It was a Chancellor’s Foot Sub.

⁷⁷ Id. at *5.

The Supreme Court’s decision in AT&T Mobility, LLC. v. Concepcion⁷⁸ that the Federal Arbitration Act (“FAA”) preempts state laws that preclude or limit arbitration continues to be enforced and extended by the Court. To the surprise of few, the Court in 2017 invalidated a Kentucky rule requiring that a power of attorney contain a clear statement authorizing the agent to enter into an arbitration agreement on the principal’s behalf. In Kindred Nursing Centers Limited Partnership v. Clark,⁷⁹ the decedents had granted a power of attorney to plaintiffs, who had then entered into an arbitration agreement with the defendant nursing home on behalf of the decedents. Plaintiffs later sued alleging that defendant’s negligent care had caused the death of the decedents and arguing that the power of attorney was invalid because it violated Kentucky’s “clear statement” rule. Justice Kagan wrote the decision for an eight justice majority (only Justice Thomas dissented), noting that Kentucky had done “exactly what Concepcion barred” by adopting “a legal rule hinging on the primary characteristic of an arbitration agreement—namely a waiver of the right to go to court and receive jury trial.”⁸⁰

Despite the Supreme Court’s consistency, both federal and state courts continue to recognize exceptions to FAA preemption. In McGill v. Citibank, N.A.,⁸¹ the California Supreme Court held that an arbitration agreement waving the right to seek “public” injunctive relief violates California public policy and is therefore unenforceable. The decision distinguished “public” injunctive relief from “private” injunctive relief, finding that the former sought to enjoin acts that “threaten future injury to the general public” and benefitted the plaintiff only to an “incidental” degree.

The Sixth Circuit joined two other courts of appeal in finding that arbitration provisions that permit only individual arbitration of employment-related claims violate the National Labor Relations Act (“NLRB”).⁸² The Circuits are split on this issue, and the Supreme Court will hear arguments at its first session on October 2, 2017 in three consolidated cases that all raise the issue of whether the NLRB

⁷⁸ 563 U.S. 333 (2011).

⁷⁹ 137 S. Ct. 1421 (2017).

⁸⁰ Id. at 1426-27.

⁸¹ 5 Cal 5th 945 (2017).

⁸² See NLRB v. Alternative Entertainment, Inc., 858 F. 3d 393 (6th Cir. 2017). For similar decisions, see Lewis v. Epic Sys. Corp., 823 F. 3d 1147 (7th Cir. 2016) and Morris v. Ernst & Young, LLP., 834 F. 3d 975 (9th Cir. 2016).

prohibits mandatory arbitration provisions with class action waivers.⁸³ The Department of Justice’s amicus brief has argued that the NLRB does not preclude class action waivers. At the moment, the NLRB disagrees, but as membership on the board changes there may be changes to its litigation position as well. Given that this decision will likely overshadow lower court decisions, we will abbreviate our discussion of this complicated topic and wait for the Supreme Court to speak.

Finally, the Consumer Financial Protection Bureau (“CFPB”) promulgated a new rule⁸⁴ prohibiting the providers of certain consumer financial products from using arbitration clauses that bar class action suits. As of this writing, the House of Representatives voted to approve a veto of the new rule (mostly along party lines), but the measure has not yet been voted on in the Senate. Absent further Congressional action, the rule will become effective on September 18, 2017, but Congress has a few weeks after that date to act.

Moving in the opposite direction, SEC Commissioner Michael S. Piwowar has recently suggested that the SEC should drop its long-standing hostility to mandatory arbitration provisions in corporate charters, and allow public companies to preclude class actions with such a provision.⁸⁵ If this provision were favored by SEC Chairman Jay Clayton, it would pass the SEC and might block securities class actions directed against companies (and their officers and directors) adopting such a provision. It is, of course, premature to predict how many public companies would adopt such a provision by charter amendment (which institutional investors would likely oppose), but it would be comparatively simple to insert such a provision in the corporate charter of future IPO companies.

IX. Class Actions Before Administrative Agencies

⁸³ These cases are cited *supra* at note 2.

⁸⁴ 12 CFR 1040

⁸⁵ For a review of his statements and their potential impact, see “The Problems with Mandatory Arbitration of Securities Claims,” Law360, August 9, 2017.

Finally, a very new development in class actions is their spread to Article I courts. Most recently, the Federal Circuit held that administrative courts can aggregate claims. *Monk v. Shulkin*, 855 F.3d 1312, 1319 (Fed. Cir. 2017) ("We see no principled reason why the Veterans Court cannot rely on the All Writs Act to aggregate claims in aid of that jurisdiction.") Whether a class action on behalf of veterans can proceed is currently being litigated before the United States Court of Appeals for Veteran Claims. *Rosinski v. Schulman*, Vet. App. No. 17-1117. Although no formal rule permits this, some argue that the agency has the power to informally create a class action on a case by case basis.⁸⁶ For more on these developments see Michael Sant'Ambrogio & Adam S. Zimmerman, *Inside the Agency Class Action*, 126 Yale L.J. 1634 (2017).

⁸⁶ One of the authors of this memo, Alexandra Lahav, has signed an amicus brief supporting this view.